

BEFORE THE  
POSTAL REGULATORY COMMISSION  
WASHINGTON, D.C. 20268-0001

Institutional Cost Contribution  
Requirement for Competitive Products

Docket No. RM2017-1

**REPLY COMMENTS OF THE  
NATIONAL POSTAL POLICY COUNCIL**  
(March 9, 2017)

The National Postal Policy Council (“NPPC”) respectfully submits these reply comments in response to comments on Order No. 3624.<sup>1</sup> That Order initiated a statutorily required periodic review of the “appropriate minimum contribution” to institutional costs that should be required of Competitive Products, collectively, pursuant to Section 3633(b).

There is widespread recognition that the Postal Service has substantially increased its volumes, revenues, and contribution from Competitive Products over the past five and ten years. As a result, Competitive Products at present collectively contribute much more than the 5.5 percent minimum that the Commission has required since 2007.<sup>2</sup> 39 C.F.R. §3015.7(c). In the initial comments, some argued that the required minimum should be raised to match or

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<sup>1</sup> Order No. 3624 (Nov. 22, 2016) (Advance Notice of Proposed Rulemaking).

<sup>2</sup> Order No. 43, Docket No. RM2007-1 (Oct. 29, 2007); Order No. 1449, Docket No. RM2012-3 (Aug. 23, 2012) (retaining 5.5% minimum after first 5-year review).

exceed, rather substantially, the current share;<sup>3</sup> others argued that it should be raised to the 10 or 11 percent range;<sup>4</sup> and some (primarily shippers) argued that the minimum required contribution should be eliminated or set at zero.<sup>5</sup>

NPPC disagrees with the view that there should be no minimum required contribution from Competitive Products, and with the view that the minimum should be raised substantially, let alone by multiples. Instead, the Commission should either retain the current 5.5 percent minimum or raise it only modestly to a level that would not disrupt the pricing of the Postal Service's Competitive Products.<sup>6</sup>

#### **I. COMPETITIVE PRODUCTS SHOULD MAKE A MINIMUM CONTRIBUTION TO THE INSTITUTIONAL COSTS OF THE SYSTEM**

First-Class business mailers currently pay in total nearly 40 cents out of every dollar of institutional costs. This is a daunting burden from a product that the Postal Service repeatedly says is in decline. If the Postal Service and Commission are concerned about the decline in market-dominant mail volumes, they should look to Competitive Products to pick up more of the burden. Indeed,

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<sup>3</sup> *Initial Comments of United Parcel Service, Inc. On Notice of Proposed Rulemaking To Evaluate the Institutional Cost Contribution Requirement for Competitive Products*, at 23 (Jan. 23, 2017).

<sup>4</sup> *Comments of the Greeting Card Association*, at 4-6 (Jan. 23, 2017).

<sup>5</sup> *Comments of Amazon Fulfillment Services, Inc.*, at 6 (Jan. 23, 2017); *Initial Comments of the American Catalog Mailers Association*, at 2-3 (Jan. 23, 2017); *Comments of Parcel Shippers Association, et al*, at 1 (Jan. 23, 2017).

<sup>6</sup> *See Comments of the Association for Postal Commerce*, at 6-7 (Jan. 23, 2017); *Public Representative Comments in Response To Advance Notice of Proposed Rulemaking To Evaluate the Institutional Cost Contribution Requirement for Competitive Products*, at 2 (Jan. 23, 2017).

while growth in Competitive Products is important to the institution generally, its primary benefit to mailers of market-dominant products is the potential to pay a larger share of the overhead costs.

Competitive Products collectively are the fastest growing segment of the Postal Service's market, and comprise an increasing share of Postal Service revenue and volume.<sup>7</sup> In view of this growth, they should be expected to bear a share of the institutional cost burden. Some of this is the natural consequence of reclassifying products from the market-dominant side to Competitive, as it is reasonable to expect that their institutional cost contribution should accompany them. But some of this reflects the increasing importance of Competitive Products to the Postal Service as a whole.

Postal Service activities that incur institutional costs undeniably benefit Competitive Products. Although -- by definition -- institutional costs are not attributed, the substantial use Competitive Products make of common costs, such as city carrier delivery, justifies requiring them to contribute to defray those costs as well. Indeed, Competitive Products in significant measure are driving important business decisions such as the design and uses of future vehicles and clusterboxes.

Certainly the Commission should reject calls to move in the opposite direction by eliminating the minimum requirement altogether. That could easily mean, contingent upon market conditions and management decisions, that

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<sup>7</sup> See *PostCom Comments*, at 3 & 5. While the Postal Service contends its share is unchanged, the overall market has grown substantially over the past five years. *Comments of the United States Postal Service*, at 11 (Jan. 23, 2017).

market-dominant mailers would be expected to bear all of the institutional costs of the system. The Postal Service's interest in and commitment to Competitive Products warrants rejection of the notion that there should be no minimum requirement.

For similar reasons, the incremental cost test would provide a poor basis for setting a minimum. Although intended to detect cross-subsidy, that test implicitly allocates *all* institutional costs to market-dominant products subject to the monopoly. It also assumes the complete accuracy of current cost attribution methodologies.<sup>8</sup> The complexity of the Postal Service's operations renders such an assumption unlikely despite the best efforts of postal cost analysts. If current cost attributions understate Competitive Product attributable costs, then a minimum contribution of zero would mean that market-dominant products would be subsidizing the Competitive Products.

In Section 3633, Congress specifically contemplated requiring Competitive Products to make a minimum contribution. Nothing in the development of those products over the past decade warrants abandoning that requirement. The Commission should not rely solely on the self-interest of the Postal Service to ensure that Competitive Products are making an appropriate contribution to institutional costs.

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<sup>8</sup> See *Comments of Former Utility Regulators*, at 3 (Jan. 23, 2017).

## **II. THE MINIMUM REQUIREMENT SHOULD NOT BE SET AT A LEVEL THAT AFFECTS MARKET PRICING**

The Commission should set the minimum requirement at a non-zero level that reflects the increased importance of Competitive Products, but at a level that does not distort Competitive Product pricing. That level should at least be the current 5.5 percent.

NPPC agrees with commenters that observed that trying to force the Postal Service to recover more in institutional costs from Competitive Products than the market allows would be unsuccessful. The test advocated by UPS essentially sets the minimum at stand-alone costs, which are a ceiling rather than a floor, and would result in a wholly unrealistic, not to mention noncompetitive (and probably unachievable), target contribution of 29 percent.

Choking off business in the Competitive Products area from a too aggressive target contribution is not in the interests of market-dominant mailers generally, including NPPC members. Inasmuch as Competitive Products constitutes a genuine bright spot for the Postal Service, reducing its competitiveness would be folly. But as discussed in the preceding Section, eliminating the minimum requirement altogether, or setting it at zero, would ignore the importance of and the Postal Service's increased attention to Competitive Products.

Competitive Products should bear a share of the institutional cost burden. That minimum share should be at least the current 5.5 percent, which has worked well over the past decade. While in view of the growth in the package and overnight delivery markets generally, a modest upward adjustment would not

be seem unreasonable, NPPC takes no strong position on any raise beyond 5.5 percent. Any such adjustment should be to a level comfortably below the current actual contribution, lest the minimum have the effect of disrupting the Postal Service's current pricing. The success of the current 5.5 percent minimum requirement may itself be a factor that the Commission may wish to take into account.

NPPC wants the Postal Service's Competitive Products to be successful and profitable. The more successful Competitive Products are, the more they may help to alleviate the institutional cost burden borne by mailers subject to the Postal Service's monopoly. But it is difficult to perceive what value providing Competitive Products offers to the institution unless those products not only are contributing to the common costs of the enterprise, but also attract sufficient volume to make such contribution meaningful.

### **III. CONCLUSION**

For these reasons, the National Postal Policy Council respectfully urges the Commission to set the minimum "appropriate share" of institutional cost

contribution from Competitive Products at the reasonable, non-zero level of 5.5 percent or modestly greater.

Respectfully submitted,

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